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IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

No. 73-971

D. C. TRANSIT SYSTEM, INC.,
Petitioner,

v.

DEMOCRATIC CENTRAL COMMITTEE OF THE DISTRICT OF COLUMBIA, BLACK UNITED FRONT, WASHINGTON METROPOLITAN AREA TRANSIT COMMISSION,
Respondents.

MOTION OF POTOMAC ELECTRIC POWER COMPANY FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND BRIEF *AMICUS CURIAE* IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

JACK E. McGREGOR
EDWARD A. CAINE
1900 Pennsylvania Avenue, N.W.
Washington, D.C. 20006

Attorneys for Amicus Curiae

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Comes now Potomac Electric Power Company (Pepco) and, pursuant to Rule 42 of this Court's Rules, moves this Court grant Pepco leave to file the accompanying brief *amicus curiae* in support of the Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit filed this day by D.C. Transit System, Inc. to review the opinions and judgments of the Court of Appeals rendered on June 28, 1973 in *Democratic Central Committee of the District*

of Columbia v. *Washington Metropolitan Area Transit Com'n*, No. 21, 865, *Democratic Central Committee of the District of Columbia* v. *Washington Metropolitan Area Transit Com'n*, No. 24,398, and *Black United Front* v. *Washington Metropolitan Area Transit Com'n*, No. 24,428. In support of its motion, Pepco submits that it has a direct and substantial interest in the outcome of this litigation. In support whereof, Pepco shows as follows:

In reversing orders of the Washington Metropolitan Area Transit Commission there under review, the Court of Appeals has held as a general proposition that a utility, notwithstanding the fact of ownership, which sells or otherwise disposes of its land out of Utility Property as no longer used and useful in the utility enterprise does not automatically receive the benefit of any appreciation in the value of land; but that depending upon the circumstances of the case the ratepayers may receive this benefit through lower rates. Pepco submits this proposition is erroneous and that if it were used as general precedent in regulatory practice, it would have a seriously deleterious effect upon the utility industries.

Pepco submits that it is significant that the doctrinal change from the constitutional requirement of fair return on fair value for utility ratemaking purposes was not argued to the Court save in Pepco's statement *amicus curiae* in support of rehearing or rehearing *en banc*, but that an analysis of that doctrinal change in economic regulation and public economic policy forms the single underpinning of the Court of Appeals' general proposition as stated above. Pepco submits that the granting of leave to file the accompanying brief *amicus curiae* will therefore result in more balanced argument to this Court on the constitutional issue here presented.

Pepco is regulated as to its rates for the retail sale of electric energy in the District of Columbia by the Public Service Commission of the District of Columbia, which, under the name of "Public Utilities Commission," is the predecessor of the Washington Metropolitan Area Transit Commission. Pepco's

rates so regulated must provide a reasonable opportunity to earn a fair return upon the fair value of Pepco's property used and useful in the utility enterprise. The Public Service Commission insofar as its regulation of Pepco has adopted the Federal Power Commission's Uniform System of Accounts Prescribed for Class A & B Public Utilities and Licensees. This system is in all material respects the same as the Uniform System of Accounts adopted by the Washington Metropolitan Area Transit Commission.

The Court of Appeals has raised a question of seriously adverse impact to Pepco, and to other utilities similarly situated, by overturning consistently applied administrative accounting practice which is the same as that employed by all other federal rate regulatory agencies of similar nature. Furthermore, retroactive application of the Court's novel precepts as to nondepreciable assets underscores the importance of these cases on the petition for the writ of certiorari.

Although the Court of Appeals no longer hears appeal from orders of the Public Service Commission or the Washington Metropolitan Area Transit Commission, it does receive petitions for review of final orders of the Federal Power Commission. It is therefore particularly significant that the Federal Power Commission has recently ruled on point that ratepayers have no interest in the property of public utilities pursuant to the Federal Power Act, 16 U.S.C. §791, *et seq.*[1] The *Duke Power Case,* which includes at least two other significant issues, is presently before this very same Court of Appeals on petitions for review.[2] Therefore, panels of the Court of Appeals may initially split on the issue before this Court on the petition for certiorari, or the issue will be decided against the Federal Power Commission and thereby directly affect

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[1] *Re Duke Power Company,* 48 FPC , , 97 PUR 3d 396, 405-406 (1972).

[2] *Electricities of North Carolina* v. *Federal Power Com'n,* D.C. Cir. Nos. 73-1185 and 73-1237, petitions for review filed February 16 and March 6, 1973, respectively. The proceeding has not yet been set down for oral argument.

every Public Utility and Natural Gas Company pursuant to the Federal Power Act, *supra*, and the Natural Gas Act, 15 U.S.C. §717, *et seq.*, in the country. In any event, the Federal Power Commission, relying upon its disposition of the issue in the *Duke Power Case*, has reaffirmed its position on the treatment of appreciation in the value of land assets by rulemaking.[3]

WHEREFORE, Pepco urges this Court grant Pepco leave to file the accompanying Brief *Amicus Curiae* in Support of Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit in order that this Court may receive, *inter alia*, argument as to the relevance of the doctrine by which the Court of Appeals underpins its general constitutional proposition, hereinbefore stated, as to increases in the value of land.

Respectfully submitted,

Edward A. Caine
Of Counsel

Jack E. McGregor
Edward A. Caine
1900 Pennsylvania Avenue, N.W.
Washington, D. C. 20006

Attorneys for Potomac Electric Power Company,
Amicus Curiae
Washington, D. C.
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[3]Order No. 473, Docket No. R-412, 49 FPC , 38 F.R. 4947 (February 15, 1973).

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BRIEF *AMICUS CURIAE* OF POTOMAC ELECTRIC POWER COMPANY IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

INTEREST OF *AMICUS CURIAE*

The interest of the *amicus curiae* is set forth in the motion which this brief accompanies. All references to the opinions below are cited to pages of Petitioner's appendices accompanying the petition for a writ of certiorari.

ARGUMENT

On June 28, 1973, the United States Court of Appeals for the District of Columbia handed down six decisions relating to nine dockets on petitions for review of several Opinions and Orders of the Washington Metropolitan Area Transit Commission (Commission), all final orders relating to rate cases of D.C. Transit, Inc. (Petitioner). The question dealt with here, relating to two of these decisions, is whether upon sale or other disposition of land out of Utility Property used and useful in the utility enterprise, the benefit of any appreciation in market value over original cost at the time of sale or other disposition must or may accrue to the investor or the ratepayer. This broad question was answered by the Court of Appeals in the following manner:

a. the fact of ownership of the property does not necessarily mean the investor is entitled to the appreciation; therefore, the determination must be according to where lie the "equities" of the case;

b. gain follows risk of loss, and benefit follows burden.

The proposition of the Court of Appeals relating to disposition of capital gains on land is of extraordinary importance. Although the Court in large measure intimately relates the parameters of the question to D.C. Transit's franchise and the resulting congressional requirement of the track-removal program, nowhere is it clear that this proposition went off on its relation to that program. Nor could it be entirely, for the Court of Appeals preliminarily answers the general question of who benefits from capital gains on land by finding generally that the owner does not necessarily so benefit. Accordingly, it may be argued that these opinions form precedent not only as to the latter general proposition but also as to disposition of the "equities", even when the facts of the case should strongly limit similar disposition.

Pepco submits that the Court of Appeals' reasoning as to the disposition of appreciation in the value of land assets is eminently incorrect and that the Court's discussion of the doctrine of fair value for ratemaking purposes, which is the Court's only support for the latter disposition, is entirely

inappropriate. Therefore, Pepco submits that to force an accounting of any such appreciation to the benefit of the ratepayer contravenes the Fifth Amendment of the Constitution and is otherwise insupportable in law or equity.

As to the petition for a writ of certiorari, Pepco submits that it is significant that the doctrinal change from the constitutional requirement of fair return on fair value as delineated in *Smyth* v. *Ames*, 169 U.S. 466 (1898), was not argued to the Court of Appeals whatsoever until Pepco filed its statement *amicus curiae* in support of the petition for rehearing and suggestion for rehearing en banc, but that an analysis of that doctrinal change in economic regulation and public economic policy forms the single underpinning of the Court's general determination. Neither Pepco nor other utility enterprises were accordingly aware of the imminent forthcoming of the Court of Appeals' disposition in the face of some 100 years of consistent treatment throughout the United States on all regulatory levels.[4] Accordingly, Pepco only sought (and was granted) its *amicus curiae* status before the Court of Appeals in the rehearing stage. Pepco now submits that this Court should grant the petition of D.C. Transit, Inc. for the issuance of the writ in order to review the Court of Appeals' holding relating to the constitutional issue of the disposition of capital gains on land belonging to a public utility when the land is transferred out of Utility Property and is no longer reasonably used and useful in the utility enterprise.[5]

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[4]See separate opinion of Judge MacKinnon, App. A, p. 100a.

The precedent against the Court is enumerable although not susceptible of specification, for throughout the United States the opposite result has been so naturally ingrained that the issue was apparently litigated only twice (App. A, pp. 17a-20a) and each went off on the system of accounts used in the particular jurisdiction. Administrative decisions in the District of Columbia have uniformly held the utility is entitled to the benefit (App. A, p. 23a).

[5]See page 3, *supra*, where in the accompanying motion Pepco discusses the significance of the Federal Power Commission's holding in *Re Duke Power Company* and the subsequent petitions for review lodged in the Court of Appeals.

I

CONFISCATING UTILITIES' PROPERTY IN THE FORM OF APPRECIATION IN THE VALUE OF THEIR LAND ASSETS BY REDUCING OTHERWISE JUST AND REASONABLE RATES CONSTITUTES TAKING WITHOUT DUE PROCESS AND WITHOUT COMPENSATION.

The Court of Appeals devotes many pages of opinion to a discussion of the doctrinal change in economic regulation resulting from the change in definition of the constitutional necessity for the reasonable opportunity of a public utility to earn a fair return on fair value. The Court concludes that therefore the benefit of appreciation in land values may accrue to the ratepayers rather than the investors. The Court further concludes that, "the doctrinal consideration upon which pronouncements to the contrary have primarily rested has lost all present day vitality" (App. A, p. 27a). Nevertheless, Pepco submits that the doctrine of fair value enunciated in *Smyth* v. *Ames*[6] and in effect withdrawn after many years by *Federal Power Com'n* v. *Hope Natural Gas Co.*[7] is entirely inapposite to the question before the Court of Appeals as well as the basic question before this Court.

Smyth v. *Ames* stood for the proposition that a utility was entitled to a reasonable opportunity to earn *from its ratepayers* a fair return upon the fair value of its property used and useful in the utility enterprise at the time of its use.[8] The only relevant change in that doctrine effected by *Hope Natural Gas* is

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[6] 169 U.S. 466 (1898).

[7] 320 U.S. 591 (1944).

[8] 169 U.S. at 546; *San Diego Land & Town Co.* v. *National City*, 174 U.S. 739, 757 (1899).

that original cost may form the base against which the fair return is calculated, for "fair value is the end product of the process of ratemaking not the starting point as the Circuit Court of Appeals held" (320 U.S. at 601).[9] As a constitutional proposition, fair value for ratemaking purposes may be held to be original cost.

Left entirely unaffected by *Hope Natural Gas*, as well as *Southwestern Bell*[10] and *Natural Gas Pipe*,[11] is the fact that the doctrine only mandates the obligation of the ratepayer to pay a reasonable sum for usage of the asset.

Therefore, the utility is entitled to a reasonable opportunity to recoup the cost of service *from the ratepayers* who occasion the cost. No more, but no less, is required of the ratepayer, the Court of Appeals' assertion to the contrary notwithstanding (App. A, p. 35a). It does not follow by any means that the ratepayer is then entitled to capital gains on property purchased by the utility for use in the utility enterprise. Capital gains simply do not form part of the cost of service and that is the reason ratepayers need not pay for the use of assets based upon their value. Accordingly, since the capital gains have only to do with the fact of ownership, the utility is entitled to the benefit thereof.

Pepco submits that the Court of Appeals erred in concluding, as it does (App. A, pp. 31a-32a), that if a utility possesses an indefeasible right to the appreciation in value of

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[9]Par. 7 of the Public Service Commission Law of the District of Columbia creates the District of Columbia a fair value jurisdiction as to regulation of electric, gas, and transportation enterprises, 43 D.C. Code §306. Fair value for ratemaking purposes in this jurisdiction is original cost.

[10]*Missouri ex rel. Southwestern Bell Tel. Co.* v. *Public Serv. Com'n*, 262 U.S. 276, 289 (1923), concurring opinion of Justices Brandeis and Holmes.

[11]*Federal Power Com'n* v. *Natural Gas Pipeline Co. of America*, 315 U.S. 575 (1942).

the utility's operating assets, then the rate base "could be set only at the true value of the assets." As previously set forth herein, the cases only show the *ratepayer* need only pay return on the capital originally invested in the asset. Nowhere did the cases purport to defeat the incidence of ownership of the land asset in the utility, and thus it does not follow that if the ratepayer need only pay for use of the asset, the utility can only recoup its toll for usage.[12]

Pepco submits that the Court of Appeals misapprehends the purport of *Board of Public Util. Com'ers* v. *New York Tel. Co.*, 271 U.S. 23, 31-32 (1926), where the Supreme Court stated on point that, "By paying bills for service [the ratepayers] do not acquire any interest, legal or equitable, in the property used for their convenience or in the funds of the company" (See App. A, pp. 20a-21a, 29a). Public utilities do not give up any interest in their property by utilizing their property in the utility enterprise and by being subjected to utility regulation. Pepco submits that no such inference is intended by the phrase "devoted to public service".

Strictly legislative regulation of public utilities was originally enacted in the public interest to counteract the lack of competition regarding certain industries which were proven not to be able to function effectively in a normally competitive atmosphere, due to their capital-intensive nature and the comparative inelasticity of demand for their commodity or service.[13] Regulatory commissions were thereafter instituted in turn, to take the place of competition, in order to replace resulting static legislative ratemaking and service-regulation by utilizing continuous oversight within the commission's expertise. The purpose of regulatory agencies is therefore to stand in large measure between the utilities and the public as more normal competition would otherwise have stood.

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[12]The Court of Appeals' holding herein in fact defeats even the utility's entitlement to payment for use, for the offset of the benefit to ratepayers against their obligation to pay for use of the land asset would reduce the amount of payment effectively in some cases to zero.

[13]*Munn* v. *Illinois*, 94 U.S. (Otto) 113 (1877).

In *Munn v. Illinois*, it was said that in order to be regulated an enterprise must be affected with the public interest and in effect devoted to public service. Neither of these propositions are susceptible of definition, but each has tended to cloud the atmosphere of economic regulation even to the extent of negating to some degree the purpose of regulation, which is merely to take the place of more normal competition. Pepco submits that, in *Nebbia v. New York*, 291 U.S. 502, 533 (1934), the Supreme Court laid to rest what was intended in *Munn v. Illinois*, by which Pepco submits that the Supreme Court in *Nebbia* affirmed the underlying proposition stated above as to the purpose of regulation:

> "The statement that one has dedicated his property to a public use is, therefore, merely another way of saying that if one embarks in a business which public interest demands shall be regulated, he must know regulation will ensue."

This Court further stated that the question to be determined is whether the regulatory law possesses "a reasonable relation to a proper legislative purpose" (291 U.S. at 536). If the question is answered affirmatively, the inquiry need go no further as to whether or not the enterprise is somehow affected with the public interest or devoted to public use.

A utility enterprise is comparable to non-regulated industry insofar as the fact that utilization of assets in a utility enterprise gives no more right to its customers to any capital gains associated with that property, than utilization of assets by any industrial concern gives a similar right to its customers. As this Court held in the *New York Telephone Case, supra*, utility status does not alter this fact.

Furthermore, as to the Court of Appeals' consideration of the departure from the concept of fair value for utility ratemaking purposes, fair value was never intended to constitute fair market value.[14] Fair value theoretically was comprised of

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[14] *McCardle* v. *Indianapolis Water Co.*, 272 U.S. 400, 410 (1926); *Los Angeles G. & E. Corp.* v. *Railroad Commission*, 289 U.S. 287, 305-306 (1933); *West* v. *Chesapeake & P. Tel. Co.*, 295 U.S. 662, 672 (1935).

several factors not limited to a consideration of original cost and reproduction cost new (market value in the case of land assets). Under fair value, market value in excess thereof was treated as surplus, for even then the utility was not entitled to its toll for usage *from the ratepayer* based upon market value; for example,

> "[I]f real estate has enhanced to such an extent that a return upon its value would be in excess of the reasonable value of the use for the purposes to which it is devoted, the excess value should be treated as surplus and not as a part of the investment upon which the public is required to compensate the owner for the service of the property." (*City of Appleton* v. *Appleton Water Works Co.*, 4 Wisc. RR Com'n 501, 579 (1910); immediate predecessor of the Wisconsin Public Service Commission).

Obviously then the fair value doctrine or the change therefrom is inapposite to the issue before this Court. Surely the general proposition that investors need not in all circumstances receive the benefit of such capital gains, which the Court of Appeals sought to draw from the receding of the doctrine of *Smyth* v. *Ames*, is a *non sequitur*. The result adjudged by the Court of Appeals therefore violates the Fifth Amendment in that private property has been taken without due process and without compensation.

II

DETERMINATION OF ANY ATTENDANT EQUITIES WOULD COMMAND THAT A UTILITY NOT BE SO DEPRIVED OF ITS PROPERTY, IN THE ABSENCE OF EXTRAORDINARY CIRCUMSTANCES.

Once the Court of Appeals found by an analysis of the fair value doctrine that investors no longer automatically receive the ownership benefit of the appreciation in the value of land assets, the Court next sought the "equities" of the case. The Court first found that gain should follow risk of loss; secondly the Court found that no one bears the risk of loss as to land; and lastly the Court found that the ratepayer should receive the

benefit, for benefit follows burden.[15] On the other hand there is no necessary relation between risk of gain and risk of loss nor between benefit and burden. Pepco submits that the Court of Appeals uncritically accepted these relationships, for a utility, in the same manner as any other industrial concern, does not utilize capital assets in the utility enterprise for any other reason than to meet the demands of its customers for its commodity or service. Moreover, the Court asserted *ipse dixit* that the ratepayer bears the land burden and thus should reap the gain, when in fact the financial and operating burden of the land itself rests entirely on the utility; all the ratepayer must do is pay for the use he makes of it.

The risk of loss as to land value at the time of disposition was borne by Petitioner and not its ratepayers.[16] If the Court of Appeals were correct in stating that the gain as to land should follow risk of loss, then the gain would inure to the benefit of Petitioner. Pepco submits that it is not enough to say

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[15]The Court of Appeals may feel that the burden does not stem from the use of the land asset but from the relation of the sale to the burden of the track-removal program pursuant to the D.C. Transit franchise, but this is less than clear (e.g., App. A, pp. 2a, 26a, 51a-52a, 57a-66a, 72a, 74a, 95a-96a; and App. B, pp. 149a-151a, 161a). Nevertheless, the Court also incorrectly applies its benefit-burden theory to land transactions not related to Petitioner's obligations pursuant to the franchise (App. A, pp. 74a, 96a). In any case, it is not correct at all to state that the conversion to an all-bus system was accomplished at no expense to Petitioner (App. A, p. 61a).

[16]The Commission and its predecessor, the Public Utilities Commission, had adopted this accounting practice similar to the Federal Power Commission Systems; the risk of loss as to land is placed upon Public Utilities and Natural Gas Companies by the Federal Power Commission Uniform Systems of Accounts, which have been adopted by numerous state commissions; the Public Utilities Commission of the District of Columbia (now Public Service Commission) adopted the FPC Uniform System of Accounts for Class A and B Public Utilities and Licensees as to Potomac Electric Power Company by Order No. 4727, December 29, 1960, and Order No. 5455, Docket No. P.S.C. No. EL-1, January 29, 1971.

that during the period of time in question in this case[17] actual circumstances tended to negate risk of loss as to land in a rising market, particularly in view of the uncertain market conditions in the future. In that regard, it is interesting to note that in *Smyth* v. *Ames, supra,* and other similar cases, the arguments for original cost were made by the utilities, for the assets had often been purchased at higher cost than the then prevailing market. In any case, ratemaking is prospective only and this use of hindsight has no place in the quasi-legislative process.

In sum, it is Pepco's position *arguendo* that if the case must turn upon the equities then it is only equitable for the utility to receive the benefit of the appreciation of land value at the time of transfer, so long as the land is transferred when it is reasonably no longer used and useful in the utility enterprise, which is the uncontested circumstance in this case. Pepco submits that in analyzing the specific risk of loss and burden as to land, which lie with the utility, the Court of Appeals also failed to focus upon the fact that the utility bears the risk of loss as to the entire enterprise, including as to land, insofar as the utility's relationship with its ratepayers, for the utility only possesses the right to a reasonable *opportunity* to earn a fair return from these ratepayers:

> "The revenue paid by the customers for service belongs to the company. The amount, if any, remaining after paying taxes and operating expenses including the expense of depreciation is the company's compensation for the use of its property. If there is no return or if the amount is less than a reasonable return, the company must bear the loss. Past losses cannot be used to enhance the value of the property or to support a claim that rates for the

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[17]The period in question in these proceedings from the Court of Appeals' viewpoint appears to be 1956, when Petitioner purchased the stock of Capital Transit, until the present, rather than the relatively short locked-in period between the date of the previous Commission final rate order and those presently under review. Pepco hereinafter takes issue with the resultant retroactive ratemaking.

future are confiscatory." *Board of Public Util. Com'ers* v. *New York Tel. Co.*, 271 U.S. 23, 31 (1926).

There is thus no equity in using appreciation in the value of land properly transferred to reduce the return allowance for the future, especially when the utility has failed to realize its authorized rate of return due to attrition caused by the very rise in prices which caused the value of the land to increase, and the resulting unit cost of providing the utility commodity or service.[18]

III

BY ORDERING REPARATIONS, THE COURT OF APPEALS EXCEEDED ITS JURISDICTION.

In overturning years of use of settled legal and resulting accounting principles consistently in use across several final rate orders of the Commission, the Court of Appeals resorted to retroactive ratemaking. Pepco submits that under the equitable remedy of restitution the Court has indulged in requiring reparations – the prevention of which proposition forms one of the cardinal bases for rate regulation.[19] Moreover, of real significance is that the Court of Appeals has actually directed Petitioner to return money collected pursuant to a series of final rate orders several of which were earlier upheld by that very Court.

In short, Congress did not write the power of reparations into the statute administered by the Commission any more than

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[18]It is important to note that a utility, unlike nonregulated industry, cannot abandon its utility obligations at will because it fails to earn a fair return, and thus an unconstitutional taking results where rates are set which prevent a fair return. See *Bowles* v. *Willingham*, 321 U.S. 503, 517 (1944); *Hegeman Farms Corp.* v. *Baldwin*, 293 U.S. 163, 171 (1934).

[19]See for example, *Arizona Grocery Co.* v. *Atchison, T. & S. F. R. Co.*, 284 U.S. 370, 389-390 (1932).

it did so as to the Natural Gas Act or the Federal Power Act.[20] There is no indication that Congress intended otherwise than that the power to set rates was placed exclusively in the Commission subject to normal appellate review. Pepco therefore submits that the earlier orders were finally reviewed on appeal, and thus at most the Court of Appeals could now order refunds only to the extent the holding on the land issue involved herein affects the orders before it. Profit from the locked-in periods covered by the rate orders previously held valid cannot now be used to reduce revenue, otherwise just and reasonable, collected pursuant to any other orders.

CONCLUSION

WHEREFORE, Pepco supports the Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit and urges this Court reverse the judgments of the Court of Appeals rendered in these cases in relation to the disposition of increase in the value of land assets sold or otherwise transferred from Utility Property as no longer reasonably used and useful in the utility enterprise.

Respectfully submitted,

Edward A. Caine
Of Counsel

Jack E. McGregor
Edward A. Caine
1900 Pennsylvania Avenue, N.W.
Washington, D. C. 20006

Attorneys for Potomac Electric Power Company,
Amicus Curiae
Washington, D. C.
December 26, 1973

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[20]See *Federal Power Com'n* v. *Hope Natural Gas Co.*, 320 U.S. 591,618 (1944), and *Montana-Dakota Util. Co.* v. *Northwestern Pub. Serv. Co.*, 341 U.S. 246, 254 (1951), respectively.